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The Main Features of Germany's Economic and Financial Situation

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THE dominating factor in German economic and financial life is the all-prevailing scarcity of goods. The war has exhausted the huge reserves, visible and invisible, which had been accumulated during an unbroken period of prosperity. The blockade, which outlasted the armistice by nearly eight months, has prevented the country from replenishing her stores at a time when her currency had still some purchasing power abroad.

The peace destroyed the country's economic system, which was largely based on coal and iron, by taking away from her nearly 75 per cent of her ore supplies and by forcing her to deliver annually to France, Belgium and Italy about one-fourth of her pre-war coal supply. The result is greatly reduced production all round.

THE SITUATION AS TO FOOD AND RAW MATERIALS

German agriculture today is raising only about 60 per cent of the crops and 40 per cent of the food produced formerly—leaving out of account the ceded territories. As Germany never was completely self-supporting—about 10 per cent of her supply of vegetable food and 33 per cent of the supply of meats and fats came from abroad—her dependency on foreign markets for feeding her people has greatly increased. It has been estimated that the cost of foodstuffs, etc., necessary for sustaining the health of the people at the very low present standard of living is about $3\frac{1}{2}$ billion marks gold. The country has no longer a surplus of

agricultural produce for purposes of exchange. Before the war, Germany was a great sugar producing country, but as the soil is greatly exhausted, and as agricultural labor is scarce and expensive, and as coal is often not available when the sugar manufacturing plants want it, she can scarcely provide her own people with sufficient rations. Although a great timber country, her imports always exceeded her exports. She will now have no available surplus, even if the home demands are severely curtailed, as the quantities asked for by the Reparation Commission are so great that their execution would endanger the conservation of Germany's natural resources.

The industrial side of the picture is even more depressing. Though the farmer's output has shrunk considerably, he is very prosperous. He has made a lot of money; he has paid off mortgages and has hoarded cash; he is changing back from intensive to extensive methods of cultivation, with the object of diminishing his money risks. He has not felt the pinch, as far as food goes, and, as he is master of butter and ham, flour and fruit, he can command clothes and boots by way of barter when he is disinclined to sell his goods at food-control prices.

Many German industries worked at top speed during the war to the detriment of the physical state of their plants. No repairs were made and the result is severe physical deterioration, which in many cases may have diminished efficiency by 50 per cent. The groups of industry which are dependent

on supplies of foreign raw material came to a standstill or nearly so. They lost many of their workmen and the workmen lost their former technical skill.

The loss of Lorraine, which produced about 60 per cent of Germany's iron ore supply, has greatly crippled her chief industry. The highest producing capacity of the iron and steel plants left to Germany is about 12 million tons of iron, or about 8 million tons less than her former output. This maximum could only be reached if 12 million tons high-grade ores were imported. This cannot be done, however, on account of the high cost of importing. The yearly production will be 7 to $7\frac{1}{2}$ million tons—not enough to supply the urgent wants of the home market after setting aside the finished material, which must be exported to pay for the import of iron ores.

COAL PRODUCTION

Worst of all is the shortage of coal. All over the world the production of coal has fallen, as labor will insist on shorter hours. The eight-hour day has become the law of Germany and the miner's shift has been reduced to seven or seven and one-half hours. The total production for 1919 was only 108 million tons or 57 per cent of the former output. Though the production of lignite has increased slightly the total heat generating power of coal and lignite combined is but 57 per cent of what it was before the war, especially as, owing to inefficient labor, the quality of the coal is 12 to 15 per cent less than formerly. As a consequence there is a coal famine all over the country. Householders' supply was reduced to 51 per cent of their greatly restricted rations. From October, 1919 to March, 1920, all industries combined received but 57 per cent of their greatly reduced demands. In Novem-

ber, 1919, 8,530 industrial concerns, each with a coal consumption of over 10 tons a month, received no coal whatsoever at the risk of keeping idle nearly $\frac{1}{2}$ million workmen. If there had not been a serious shortage of raw material, which prevented many works anyhow from working their full capacity, the want of coal would have been felt much more strongly. As it was, such industries as brickmaking, which are not dependent on foreign supplies, are seriously crippled. Instead of a possible production of 25 billions they turned out only about 5 billions; hence, the impossibility of building and the perpetuation of congestion all over the cities, big and small. The seclusion of private life is no longer safeguarded, nearly every occupant of a house or a tenement has been compelled to take in lodgers.

There has been a considerable improvement in the coal situation lately, inasmuch as an output of about 126 million tons may be expected for the current year, due to the increased number of miners and the extra shifts worked by them. This improvement will be offset completely by the enforcement of the Spa agreement, which will take from Germany 24 million tons of coal a year. As this does not constitute the possible maximum—which is at present about 39 million tons a year—set down in the Peace of Versailles, every additional ton mined by Germany may be taken away from her. The energy of the miners is paralyzed, the scarcity of coal is perpetuated, thus causing the shortage of the entire industrial production.

This scarcity of coal is made quasi-permanent by the lowered efficiency of labor. The war and the blockade have gravely affected the stamina of the working class. Notwithstanding a shorter working day, the output of the coal in the Ruhr district per hour has

fallen from 136.3 kilograms per head in 1913 to 127.5 kilograms per head in July–December, 1919. If the working hours had not been reduced after the revolution, the decline in the worker's efficiency would have been much greater. The reduction of the working hours has made it possible, too, in many cases to carry on work with a very insufficient supply of raw materials. It has greatly lessened the danger of unemployment, as many more men are wanted to do the same amount of work; but, as it cannot be accompanied by better organization under present circumstances, nor by increased personal efficiency, it has raised the cost of production.

German industries are carried on at half speed; the producing capacity cannot be thoroughly utilized as the output is insufficient. Thus, the cost of the finished article is raised proportionately. The carrying out of the Spa agreement will reduce the coal supply of industry by another 16 per cent; it may diminish the output by nearly double the amount and raise the cost of the remaining production correspondingly.

THE FINANCIAL SITUATION

The scarcity of goods on the one side is accompanied by a redundancy of currency on the other side.

The German government has financed the war mostly by issuing loans. On account of the blockade, customs brought in very little, and on account of the scarcity of goods, consumption could not be fairly taxed. The result was a huge increase of the debt. It rose from 22 billion marks, Reich and States combined, to 247 billion marks, for the Reich. More than half of this debt—132 billions—is short-termed floating debt, which cannot be funded at present, as there is little chance of placing a big loan with the public.

Whenever these mature they have to be renewed. They are mainly treasury bills which the "Reichsbank" discounts, issuing notes for them. So far, the bank has been able to sell about half the treasury bills to the public and the other banks. Whenever there is a severe stringency of the money market, however, the banks must unload their holdings for rediscount on the Reichsbank, which must issue notes against them. If the nearly 50 billion marks treasury bills held by the banks at the end of March were to return suddenly to the Reichsbank, the note circulation would be immensely increased. So far, the government has paid its way by the issue of these treasury bills and only indirectly by the issue of bank notes. As long as some of the bills are taken up by the Joint Stock Banks, the note circulation of the Reichsbank will be smaller than the floating debt.

On August 30, 1920, the total paper circulation was over 72 billion marks, including nearly 14 billion marks in loan certificates. It is increasing rapidly since, partly because public income does not yet meet public expenditure and partly because of the necessity forced upon the bank to buy foreign bills of exchange for payment of foreign debts.

Very little gold—only about 1 billion marks—is left to the bank. The amount of notes outstanding at the beginning of spring was about twenty-four times the amount outstanding on June 30, 1914. These figures give quite a misleading impression, even if the amount of gold withdrawn from circulation since 1914 were properly accounted for, for between 20 to 25 billion marks notes do not circulate within the country. They are held abroad, partly in France and in Belgium as a result of the German occupation during the war and partly in other countries as a result of speculation

for the rise of the mark. These notes do not swell circulation but they form part of a foreign debt which may be called in without notice to the great detriment of the German exchange.

GERMAN EXCHANGE

German exchange is in a very precarious situation. Since Germany has been deprived of her merchant marine and of the greater part of the property of her nationals situated in allied territory, her exports are her only means to pay for her imports. Her exporting capacity is greatly diminished by the scarcity of goods mentioned above, while her demand for imports is almost unlimited. The value of imports for 1919 is estimated at 32 billion marks paper, that of exports at 10 billion marks. There was an unfavorable balance of over 22 billion marks to settle. The imports for the next years may reach about 80 billion marks; the exports about 35 to 40 billion marks, so there will be an unfavorable balance of about 40 billion marks.

This being so, the German exchange must be unfavorable as there is no gold, nor sufficient securities, nor long-termed credits available to equalize the supply and the demand for foreign bills. The outcome of this was the catastrophic fall of the German exchange, from about 12 marks the dollar in the summer 1919 to about 100 marks in the first days of March; it has since risen again to 39 marks, and fallen again to 61 marks, as the decline was out of all proportions to the intrinsic value of the mark.

A permanent rise is not very likely so long as the balance of trade is unfavorable and so long as the state of public finance is unsatisfactory.

INCOME FROM TAXATION

The estimates for the present year for the Reich look forward to an ex-

penditure of 100 billion marks; two-thirds of it, about 60 billions, must be provided for from loans. Of this expenditure 60 billion marks are non-recurrent, 18 billions of this are due to the loss on the state railways and the post-office. It will not be possible to do away with those deficits as long as prices are high and as wages have to be raised correspondingly. Recurrent expenditure is estimated at nearly 40 billion marks, of which about 12 billion marks are for the service of the debt. A great many new taxes weighing heavily on income and on property have been granted, but their proceeds are coming in very slowly.

The total yield of taxation will bring in about $37\frac{1}{2}$ billion marks when all taxes are properly established. In the proceeds of these taxes the states and the municipalities have a share of about $9\frac{1}{2}$ billions. Their permanent expenditure is 26 billions, 23 of them permanent, so new taxes must be resorted to. While taxation before the war averaged about 50 marks per head, it has now reached an average of 629 marks. As the total expense of the central government is 1955 marks per head further heavy taxation is unavoidable. Incomes have grown of course with the spread of inflation but not at the same speed. The income of the officials of the Reich is a little more than five times their pre-war income.

Though taxation will be very heavy, it could be borne if production were in full swing. If that were the case incomes would be real incomes, not merely nominal. The cost of living would fall and the margin available for taxation would rise. Public services could be cheapened and worked at profit. Though railway rates have been raised nearly six times their former standard, the systems are worked at a loss, as the high rates have reduced

traveling, and as the cost of operating is rising rapidly.

EFFECTS OF THE PEACE TREATY

At present the Peace of Versailles and its result bar the way to recovery. The foundation of German production is coal. So long as the country is made to pay coal instead of settling its objections by selling products made with coal, her industries cannot work at top speed, her exports cannot rise, her exchange must fall and prices must go on soaring.

Germany is forced to make reparation in such a way as to diminish her capacity for paying at all. Unwarranted fears of her planning a coal monopoly—she is by no means the only coal producer on the continent—and the spectre of her dumping finished goods are invoked as reasons for forcing the exports of coal rather than of highly finished manufactured goods. The result must be a continued fall of her exchange which may bring about such a premium on exports as to seriously disturb competing industries of other countries. The financial obligations of the Peace of Versailles are working in the same direction. The ships which Germany has delivered, the coal she has given up, the property of her nationals, the cost of the material for reconstruction, must be paid to the German nationals by the German government. Goods to the value of 20 billion marks gold, nearly 5 billion dollars, must be paid up to May 1, 1921. Most of these have been handed over to the Allies but the question of financing these deliveries from the Treasury remains. Her funded debt is above 91 billions, her floating debt 136 billions. How can Germany do it? Twenty-five billion marks for carrying out the Peace Treaty appear in this year's revised estimates. The total compensation which the Reich will be expected to pay the nationals is

estimated at 131 billion marks, omitting the 90 billions for liquidated property, 17 billions for the cession of the ships of the Merchant Marine. She cannot do it with the proceeds from her taxes, for the available taxes are not yet sufficient to meet the current expenditure. She must borrow money. She cannot place funded loans on the market, for just now there is a scarcity of capital which will be greatly increased by the huge inroads of the tax collector and by the further spread of inflation. No surplus capital for long-termed investments will be available. So Germany must increase her floating debt. This means a new issue of bank notes in the long run and an increased issue of bank notes means inflation. Inflation must bring about a rise in prices, a rise in wages, a scarcity of working capital, increased government expenditure and a falling exchange.

It is right and proper for Germany to pay the reparations she has agreed to pay, but she ought to do so at a time when her resources permit it and in such a way as to safeguard her productive capacity. At present the payment of her reparation debt is arranged in such a way as to be heaviest when her resources are smallest. She has been compelled to hand over working capital to the Allies up to the value of 20 billion marks gold within eighteen months at a time when her financial strength is nil. She is forced to hand over the proceeds of the German liquidations and renounce the right of her nationals in their property held abroad. She is expected to compensate them. As the value of their property has been estimated at above 20 billion marks gold, just compensation for this item alone would amount to 200 billion marks paper. This payment may be spread over many years

and it may be heavily taxed. It will always be a burden which cannot be financed at present according to any known rule of sound finance. And it is only one item of the bill for coal, dyestuffs, timber and new ships will have to be delivered at stated intervals. They must be paid for by the public purse. Germany must pay in goods so long as goods are scarce and essential for the reconstruction of European business life. Later on, when they are a drug on the market and when they cannot be sold, she may keep them but she must pay an annuity in gold from the disposition of unsalable goods. She could pay handsomely if she were permitted to work at full speed; but how can she pay when her working capacity is crippled? A semi-savage country can pay in raw material; a congested country with a complex social organization can only

pay with such finished articles as she is allowed to produce.

As long as reparation is not settled on such a basis as to make sound financing possible, no amount of taxation and no heroic measures can save German public finance. No levy on capital, no forced loan will do any permanent good, for as soon as one part of the floating debt has been funded at a heavy sacrifice and as soon as new issues have been stopped temporarily, a new demand for huge sums is bound to arise which can only be provided for by new issues of short-termed bills. The financial clauses of the Peace Treaty stand for "Fiat Money." The authors must have had an almost wonderful belief in the financial genius of German financiers or a miraculous faith in the possible achievements of the printing press issuing bank notes.